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C O N F I D E N T I A L SECTION 01 OF 03 TAIPEI 003930

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TAGS: EINV ECON ETRD TW CH
SUBJECT: CROSS-STRAIT INVESTMENT KEEPS GROWING

Classified By: AIT Director Douglas H. Paal, Reason 1.5 D

Summary

¶1. Taiwan investment in the PRC approved by Taiwan's Ministry of Economic Affairs during the first six months of 2004 was 68 percent higher than the same period last year. PRC data also shows a substantial increase in contracted investment but a modest drop in realized investment. High-tech firms lead the trend, but firms in heavy industries, including steel and cement, are also investing in the PRC. Taiwan investment is concentrated in the Pearl and Yangtze River Deltas areas, with investment in the Yangtze Delta region growing faster. Nevertheless, Taiwan's restrictions on certain categories of investment continue to hold back Taiwan firms in the high-tech industries where Taiwan's advantage is strongest. End Summary.

Taiwan's Mainland Investment Continues to Grow
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¶2. (U) Recent statistics released by Taiwan's Ministry of Economic Affairs (MOEA) show that Taiwan's investment in the PRC continued to grow during the first half of 2004 at a remarkable pace. MOEA approved USD 3.39 billion worth of investment during the period. This represents a 68 percent increase over the same period in 2003. Investment in Mainland China accounted for at least 70 percent of Taiwan's total foreign investment during the first half of the year. Some officials estimate that up to 75 percent of Taiwan's investment goes to the Mainland if money funneled through offshore financial centers such as the Cayman Islands is included. According to MOEA, Taiwan's cumulative investment in the PRC increased 9.9 percent during the period to USD 37.7 billion. Most observers believe that a large portion of Taiwan's investment in the Mainland evades MOEA approval. Unofficial estimates of Taiwan's cumulative investment in the PRC range as high as USD 190 billion.

¶3. (C) The PRC Ministry of Commerce's data for the first half of the year as re-released by Taiwan's MOEA show a somewhat different story. The PRC provides data on contracted and realized investment. The total value of contracted investment for the first six months of 2004 increased 31.6 percent to USD 4.66 billion. However, the value of realized investment)- dollars actually spent -- declined 10 percent compared to the same period in 2003 to USD 1.89 billion. Taiwan MOEA's Investment Commission Executive Secretary Huang Chin-tan speculated to AIT/T that the decline in realized investment during the period was probably due to the PRC's political pressure on "pro-green" investors who support Chen Shui-bian's Democratic Progressive Party and the PRC's macroeconomic control measures aimed at slowing China's growth. Huang expects realized investment figures to show growth again in 2005.

High Tech Industries Lead the Trend

¶4. (U) High tech firms continued to dominate Mainland investment during the first half of the year. According to MOEA, electronics and electrical appliance manufacturing accounted for just over 50 percent of Taiwan's investment in the PRC. Several large-scale high tech investments made up a particularly large portion of Mainland investment approved by MOEA during the period. Taiwan Semiconductor Manufacturing Company's (TSMC) plan to invest USD 371 million in an eight-inch semiconductor foundry near Shanghai was approved. In addition, MOEA authorized Hon Hai Precision, manufacturer of a range of IT equipment and components, and TFT-LCD producer AU Optronics to invest USD 57.4 million and USD 100 million respectively.

¶5. (C) Taiwan's heavy industry firms are also continuing to invest in the Mainland. Together, investments in basic metals and metal products, non-metallic minerals (including cement), and chemicals accounted for 18 percent of approved investment during the first half of 2004. Among the largest, MOEA approved Formosa Chemicals and Fibre Corp.'s plan to invest USD 48.3 million in a petrochemicals plant and Yieh United Steel's plan to invest USD 51 million in a stainless

steel project. These results seem surprising given the PRC's efforts to slow down its economy, in part aimed at the construction industry. Even industries that would be most susceptible to these economy-cooling measures have seen large new investments. MOEA approved Taiwan Cement's plan to invest USD 50.8 million in the first half of the year. Furthermore, in the second half at least three additional large-scale investments in the cement industry have also been approved. MOEA's Huang told AIT that his office contacted steel and cement industry investors and learned that the PRC approved their investments despite efforts to slow the economy because the projects would improve energy efficiency in the PRC.

Taiwan's Investment in the PRC Moving North

¶6. (U) Taiwan's investment in the Mainland is mostly clustered in the Pearl and Yangtze River Delta areas. However, the latest data from MOEA suggest that investment in the Mainland is moving north. Whereas Guangdong and Fujian provinces accounted for about 39 percent of investment approved up through 2003, they made up only 25 percent of investment approved during the first half of 2004. Jiangsu and Zhejiang provinces together with the municipality of Shanghai, on the other hand, accounted for more than 68 percent in the first six months of the year, compared to only 47 percent of cumulative investment through 2003. The conventional wisdom is that Taiwan's high tech firms tend to invest in the Yangtze River Delta area, while manufacturers of other consumer goods, such as textile, toy, and shoe manufacturers, tend to concentrate along the Pearl River in cities like Shenzhen and Dongguan, Guangdong province. MOEA's data bear this out. Approximately 75 percent of Taiwan's approved investment in the electronics and electrical appliance category was destined for the Yangtze River Delta area during the first half of 2004.

Investment Policy Still Impedes Some Investment

¶7. (C) Even as investment in the Mainland rises rapidly, Taiwan's regulations continue to prevent some investment. Taiwan's government has been considering for sometime lifting investment bans for small TFT-LCD panel manufacturing, integrated circuit (IC) packaging and testing, and trash incineration. Pre-election politics have delayed approval of these categories, but according to MAC officials, these categories will be approved for investment around the end of the year. Several firms have expressed interest to MOEA and are ready to invest in these categories. Other categories, notably large TFT-LCD panel and advanced semiconductor manufacturing, remain prohibited with no sign that the Taiwan government will lift restrictions in the near future.

¶8. (C) Taiwan is moving slowly to liberalize semiconductor investment in the Mainland. It has already decided to allow up to three firms to build eight-inch wafer semiconductor foundries in the PRC. So far, only TSMC has been approved. In addition, United Microelectronics Corp., Powerchip Semiconductor Corp., ProMos Technologies Inc., and Nanya Technology Corp. have all expressed interest in building foundries in the Mainland. The Taiwan government still prohibits investment in the Mainland in the more advanced twelve-inch wafer technology. However, it has not succeeded in keeping this technology out-of-reach for PRC manufacturers. In September, the PRC's Semiconductor Manufacturing International Corporation (SMIC) opened its first twelve-inch wafer manufacturing facility in Beijing. As reported in the media, Taiwan PC manufacturer Acer Chairman Stan Shih argues in his new book "Millennium Transformation: Change Management for New Acer" that it's too late for Taiwan firms to dominate the PRC chip market. He believes that had firms like TSMC been able to invest in the Mainland sooner they would have been able to eliminate competition from PRC-based firms. He believes that PRC firms have now attained a level of technology that will make them strong competitors. TSMC blames, at least in part, industrial espionage for SMIC's success. TSMC has filed suit against SMIC for patent and trade secret infringement with the U.S. District Court for the Northern District of California and the U.S. International Trade Commission. If Taiwan continues to hold back the industries where its competitive advantage is strongest -- like semiconductors -- it will face increasing competition from the PRC and other countries and risks its own future growth
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